No. 427

IN THE

Supreme Court of the United States

OCTOBER TERM, 1939

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

ALFRED C. FULLER

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

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BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 45-51) is unreported. The opinion of the Circuit Court of Appeals for the Second Circuit (R. 57-58) is reported in 105 F. (2d) 903.

JURISDICTION

The judgment of the Circuit Court of Appeals (R. 58) was entered July 19, 1939. The petition for a writ of certiorari was filed September 29, 1939 (R. 58) and granted on February 5, 1940 (R. 58). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The question presented is whether the income for the taxable years 1931, 1932 and 1933 from an irrevocable trust created by the respondent Fuller, pursuant to agreement looking to a divorce by his wife, which she later obtained, is taxable to him although he received none of the income from the trust and had no participation whatsoever, either present or prospective, in either the income or principal thereof, and although the income from the trust was not used to satisfy any legal obligation, contractual or otherwise, of his, to support, maintain or pay money to his divorced wife in any of the taxable years involved.

STATUTES INVOLVED

The statutes involved are set forth in the appendix, infra, pp. 17 to 20.

STATEMENT

The facts as stipulated (R. 18-31) and found by the Board of Tax Appeals (R. 45-48) may be summarized as follows:

On July 25, 1930 the respondent, Alfred C. Fuller, and his then wife, Evelyn W. Fuller, executed a written agreement (R. 20-24) which in its preambles recited that the parties intended thereby to adjust, settle and determine their respective rights and duties as to the support and maintenance of Mrs. Fuller and the rights of each in and to the property of the other, if any, in lieu of a judicial determination thereof in a contemplated divorce action (R. 20).

The agreement expressly provided that both of the parties, in consideration of the covenants therein and the performance thereof, waived and surrendered all their respective rights in and to the property of the other, including the right of support, and all claims which either had or might have against the other on account of their then marital relationship (R. 24).

In said agreement respondent agreed to transfer certain shares of stock of the Fuller Brush Company in escrow (R. 21) and upon issuance of a divorce decree to establish an irrevocable trust of said stock for a period of ten years, the income therefrom to be for the maintenance and support[1] of Mrs. Fuller, or in case of her death, for the maintenance and support of the two sons of the Fullers, or in case of the death of both of the sons and in the absence of a will of Mrs. Fuller, for the maintenance and support of her heirs (R. 22). The agreement further provided that upon the expiration of the ten year period the trust should terminate and the principal, together with all accumulated dividends, interest, rights and income

[1] The words "maintenance and support" are merely terms of art requisite to the creation of a spendthrift trust. (R. 29, 30.) Sec. 5723 Conn. Gen. Stat. Rev. 1930. See Appendix, p. 20 infra.

not previously paid out should become the absolute property of Mrs. Fuller free of the trust (R. 22).

On November 12, 1930 the Second Judicial District Court of the State of Nevada in and for the County of Washoe entered its findings and final decree of divorce in favor of Mrs. Fuller (R. 25, 26). The Nevada court included in its Findings the fact that the agreement of July 25, 1930 had been entered into and its decree was in the following form (R. 26):

> "Ordered, Adjudged, and Decreed that the plaintiff be, and she hereby is, granted a divorce from the bonds of matrimony existing between the plaintiff and the defendant and that said parties be and they hereby are restored to the status of single persons.
>
> It is further Ordered, Adjudged and Decreed that said agreement entered into between the plaintiff and the defendant on or about the twenty-fifth day of July, 1930 be and the same hereby is approved."

On December 22, 1930 the respondent, his divorced wife and The Hartford-Connecticut Trust Company entered into an agreement of trust (R. 28-31). The trust agreement expressly provided that it was entered into in order to reaffirm the terms of the agreement of July 25, 1930 and to effectuate said agreement. The trust was irrevocable and was to continue for a period of ten years from November 12, 1930 regardless of any change thereafter in the Trustees, the beneficiary or the principal of said trust (R. 28).

In accordance with the trust agreement, the Trust Company as Trustee received from The Fuller Brush

Company all the dividends and income from said shares of stock during the years 1931, 1932 and 1933 (R. 19) and all of said dividends and income so received were paid out to or disbursed for the benefit of Mrs. Fuller by the said Trust Company (R. 19).

The respondent did not include this income in his tax returns for the years in question (R. 20) but the Commissioner assessed deficiencies with respect thereto (R. 7, 16). The decisions of the Board of Tax Appeals sustaining the action of the Commissioner were reversed by the Court below (R. 57, 58).

OUTLINE OF ARGUMENT

First Point

The general rule is that ownership of income, or of the property from which it accrues, determines the taxability of such income. The respondent in the case at bar has retained none of the incidents of ownership of either the income or the principal of the trust fund, the income from which is sought to be taxed to him.

Second Point

Where, pursuant to a separation agreement for the benefit of his former wife, a divorced husband has established a trust as to which he thereafter has no beneficial or property interest, present or future, in either principal or in-

come, and where he is thereafter under no continuing obligation to support her, the income from the trust paid to or for the benefit of the former wife is not taxable to the settlor.

Third Point

After the divorce decree and the establishment of the trust fund, the respondent had no further or continuing obligation to support or pay money to his former wife, and therefore her income from the trust fund is not taxable to the respondent.

Fourth Point

The property settlement was the equivalent of a lump sum settlement; the trust corpus became the equitable property of Evelyn W. Fuller, and the respondent should not be taxed on her income therefrom.

Fifth Point

The income from the trust belongs to Evelyn W. Fuller, and to measure the respondent's income in part by that earned by the trust fund would be to deprive respondent of his property without due process of law in violation of the Fifth Amendment to the Constitution of the United States.

ARGUMENT

First Point

The general rule is that ownership of income, or of the property from which it accrues, determines the taxability of such income. The respondent in the case at bar has retained none of the incidents of ownership of either the income or the principal of the trust fund, the income from which is sought to be taxed to him.

The general rule is that ownership of income, or of the property from which it accrues, determines the taxability of such income. *Blair v. Commissioner*, (1937) 300 U. S. 5; *Hoeper v. Tax Commission*, (1931) 284 U. S. 206; *Poe v. Seaborn*, (1930) 282 U. S. 101.

The respondent in the case at bar has retained none of the incidents of ownership, present or future, in either the income or the principal of the trust fund, the income from which is sought to be taxed to him. The term of the trust is for ten years from November 12, 1930. At the end of that period, the entire fund is to become the absolute property of Evelyn W. Fuller and is to be transferred to her free of the trust, or if she be not then living, the property is to pass outright by her will or to her heirs if she dies intestate. The trust is irrevocable. The respondent can under no condition recover any part of the trust fund or any of the income. If the trust income diminishes he suffers no loss and if it increases, he participates in no part of it.

Second Point

Where, pursuant to a separation agreement for the benefit of his former wife, a divorced

husband has established a trust as to which he thereafter has no beneficial or property interest, present or future, in either principal or income, and where he is thereafter under no continuing obligation to support her, the income from the trust paid to or for the benefit of the former wife is not taxable to the settlor.

This Court held in *Douglas v. Willcuts*, (1935) 296 U. S. 1 that where trust income is applied in discharge of an existing obligation of the settlor, the income remains taxable to him because the trust in such circumstances is merely a device for securing the performance of a continuing obligation. In *Helvering v. Fitch*, (1940) —U. S. —, 84 L. Ed. 399, this Court pointed out that there were three factors which made it apparent that the trust in the Douglas case "was merely security for a continuing obligation of the taxpayer to support his divorced wife". Those factors as there listed (84 L. Ed. 400) were:

1st: Douglas' "agreement to make up any deficiencies in the $15,000 annual sum to be paid her under the trust".

2nd: "The power of the Minnesota divorce court subsequently to alter and revise its decree and the provisions made therein for the wife's benefit".

3rd: "The provision (in the trust agreement) that on the death of the divorced wife the corpus of the trust was to be transferred back to the taxpayer".

Although the first and third factors were absent in the Fitch case, this Court held that the taxpayer had failed to prove the lack of power in the (Iowa) divorce court to alter or revise its decree. But the opinion makes it clear

that where (p. 403) "local law and the alimony trust have given the husband a full discharge and leave no continuing obligation, however contingent * * * income to the wife from an alimony trust (is to) be treated under the revenue acts the same as income accruing from property after a debtor has transferred that property to his creditor in full satisfaction of his obligation".

Third Point

After the divorce decree and the establishment of the trust fund, the respondent had no further or continuing obligation to support or pay money to his former wife, and therefore her income from the trust fund is not taxable to the respondent.

None of the three factors emphasized by this Court in the Fitch case as indicia of a continuing obligation is present in the case at bar.

1st: By the terms of the trust agreement, Mrs. Fuller during the taxable years in question was entitled to and did receive the net income of the trust. There was no guarantee on the part of the respondent to make up deficiencies so as to insure her receipt of a specified annual sum.

2nd: The Nevada Court retained no power to alter or revise its decree.

> "A decree a vinculo is final, and the jurisdiction of the court over the parties is after the expiration of the term at an end; and just as there can be no

> grant of alimony after such a divorce, so there can be no change in the award of alimony, unless the right to make such change is reserved by the court in its decree, as it may be, or is given by statute, as it often is. * * *. But where there is no such statute (and we have none), and where the decree does not reserve the right to the court (as it does not here) to alter the decree for alimony, no such authority exists". *Sweeney v. Sweeney*, (1919) 42 Nev. 431, 439, 179 Pac. 638, 639.

The Circuit Court of Appeals so held (*Fuller v. Commissioner*, 105 F. (2d) 903, R. 57) and that holding is not challenged in this Court.

The petitioner cannot now attack that holding for it was not assigned as error in the petition for certiorari and the question was not presented as a reason for granting the writ.[2] *Crown Cork & Seal Company v. Gutmann Company*, (1938) 304 U. S. 159; *General Talking Pictures Corporation v. Western Electric Company*, (1938) 304 U. S. 175, 305 U. S. 124.

3rd: There is no provision for reversion of the trust corpus to the settlor on the death or remarriage of the divorced wife. On November 12, 1940 the trust is to terminate and the corpus is to become the absolute property of Mrs. Fuller or if she be not then living, the property is to pass outright by her will or to her heirs if she dies intestate.

The petitioner does not dispute the absence in the case at bar of the three factors above discussed. The petitioner contends that *if* there is a legal obligation under the appli-

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[2] See the petition for certiorari, pp. 3 and 4. Contrast the petitions in *Helvering v. Fitch*, supra and *Helvering v. Leonard*, No. 426, Present Term.

cable state law to support the wife after she has obtained a divorce, and the income from a trust is devoted to the discharge of that obligation, then the amount of trust income payable to the wife is taxable to the husband whether or not the divorce court has jurisdiction to change the provisions of its decree relating to the maintenance of the wife or whether or not the wife has any recourse against the husband beyond the terms of the trust. The nature or legal basis of such an hypothetical obligation of support is not elucidated in the petitioner's brief, but reference is made to the possibility of its existence under either Nevada or Connecticut law. The vagueness of the petitioner's contention leaves the respondent in the difficult position of discussing a negative generality rather than a specific claim of law. We submit, however, that after the fulfillment of the separation agreement by the establishment of the trust, no further obligation upon the respondent to support his former wife existed or could exist either in Nevada or Connecticut or elsewhere.

So long as the marital status continues a husband is under an obligation to support his wife, but a decree of absolute divorce terminates that obligation except in so far as the divorce court otherwise decrees.

> "Unless otherwise provided by local law, a decree of divorce by a court having jurisdiction of the cause and of the parties, dissolving the bonds of matrimony, puts an end to all obligations of either party to the other, and to any right which either has acquired by the marriage in the other's property, except so far as the court granting the divorce, in the exercise of an authority vested in it by the legislature, orders property to be transferred or alimony to be paid by one party to the other." *Barrett v. Failing* (1884) 111 U. S. 523, 524-5.

There is no case or statute[3] in Nevada providing otherwise. The controlling case is *Sweeney v. Sweeney*, supra. The divorce decree in the case at bar restored the parties to the status of single persons and made no provision for alimony. It follows that the matrimonial obligation of support ceased with the termination of the matrimonial status.[4]

The decree of the Nevada court terminating the marriage relationship and restoring the parties to the status of single persons is entitled to full faith and credit in all states including Connecticut. *Gildersleeve v. Gildersleeve* (1914) 88 Conn. 689; *Sistare v. Sistare* (1910) 218 U. S. 1; *Davis v. Davis* (1938) 305 U. S. 32; *Yarborough v. Yarborough* (1933) 290 U. S. 202. Alimony can be granted only as authorized by statute. (*Schouler, Marriage, Divorce, Separation and Domestic Relations*, 6th Ed., Vol. 2, Sec. 1797.) The only Connecticut statute relating thereto (Sec. 5182 Conn. Gen. Stat. Rev. 1930, see Appendix p. 19) merely authorizes the awarding of alimony to a woman divorced by a Connecticut court. The Connecticut cases cited by the petitioner on page 5 of his brief are not in point.[5]

By the terms of the separation agreement, Evelyn W. Fuller released all rights of support against the respondent.

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[3] The Nevada statutes cited in the petitioner's brief (p. 5) and set forth in the appendix of this brief (pp. 17-19) merely authorize the divorce court to award alimony, and the Nevada cases cited by the petitioner are merely instances in which alimony was awarded in connection with the granting of a divorce.

[4] "The dissolution of the marriage relation extinguishes the subject matter which forms the basis of an action or proceeding for separate maintenance." *Herrick v. Herrick* (1933) 55 Nev. 59, 68; 25 Pac. (2d) 378. "The jurisdiction acquired by the Nevada court made the decree effective to end the marriage for all states." *Mallina v. Mallina* (1938) 4 N. Y. Supp. (2d) 27, 33.

[5] The case of *Wright v. Wright* (1919) 93 Conn. 296 held that decreed alimony not a judgment debt for the purposes of garnishment. In *Cary v. Cary* (1930) 111 Conn. 256 the Court pursuant to statutory authority modified a Connecticut divorce decree to the extent of vacating an award of monthly alimony upon the remarriage of the divorced wife.

This agreement was shown to the divorce court and approved by it, and was therefore valid and conclusive. *Maisch v. Maisch* (1913) 87 Conn. 377. The only obligation assumed by the respondent under the terms of the agreement was the obligation to establish the trust, to transfer the designated securities to the Trustees. This he performed before the beginning of any of the tax years in question. Mrs. Fuller's only rights thereafter were the property rights she acquired in the trust fund, for she voluntarily surrendered her rights against the respondent in exchange for the establishment of the trust and the creation of rights thereunder.

It is apparent that Evelyn W. Fuller could not at any time after the divorce decree was granted and the trust established force the respondent to contribute to her support either in Nevada or in Connecticut. Local law and the establishment of the trust fund have given him a complete discharge and therefore he is not liable for taxation on her income from the trust fund. See *Commissioner v. Tuttle* (1937) 89 F. (2d) 112 (C. C. A. 6th).

Fourth Point

The property settlement was the equivalent of a lump sum settlement; the trust corpus became the equitable property of Evelyn W. Fuller, and the respondent should not be taxed on her income therefrom.

The resort to the trust device was not for the purpose of securing the performance of a continuing obligation for no such obligation existed as has been pointed out under the Third Point in this brief. The respondent made an

absolute transfer and the ownership of the corpus of the trust as well as the income therefrom was finally and irrevocably renounced by him. By virtue of the Nevada decree, Mrs. Fuller became a separate and independent economic unit (Conf. *Helvering v. Clifford*, (1940) — U. S. —, 84 L. Ed. —). No one would contend that if the securities in question had been transferred outright to Mrs. Fuller free of the trust the respondent would remain liable for taxation upon the income therefrom. In such a case the property transferred becomes the absolute property of the former wife. *Cary v. Cary*, (1930) 112 Conn. 256, 259. For tax purposes the outright transfer in trust in the case at bar is no different from a lump sum settlement.

The petitioner cites in the appendix of his brief (p. 6) Article 83, Regulations 74 of the Revenue Act of 1928, which provides that an amount of principal paid under a marriage settlement is a gift and not taxable income to the recipient but that income derived from that principal is not exempt from the income tax. Inasmuch as the trust corpus became in effect the absolute property of the respondent's former wife, the income should be taxed to her.

Property settlements in connection with divorces have frequently taken the form of trust settlements and it is natural to suppose that this was true before the income tax amendment was adopted. This form of settlement gives the wife a security for the future which she would never have if she were compelled to rely on periodical payments made by the husband from his own earnings or property pursuant to a Court decree. Where such a trust settlement is made irrevocably and without any possibility of ultimate reversion to or participation by the husband, it is as abso-

lute and complete as a lump sum settlement, and for tax purposes it should be so treated. If it is not so treated, the income from the trust which regularly accrues to the former wife as beneficiary may escape taxation altogether through exigencies in the divorced husband's business or financial affairs.

Fifth Point

The income from the trust belongs to Evelyn W. Fuller, and to measure the respondent's income in part by that earned by the trust fund would be to deprive respondent of his property without due process of law in violation of the Fifth Amendment to the Constitution of the United States.

It is a fundamental proposition that to measure the income, for tax purposes, of one person by that of another, is a taking of property without due process of law. *Hoeper v. Tax Commission*, (1931) 284 U. S. 206. The respondent contends that to tax him on his former wife's income from the trust fund would be to violate that fundamental proposition.

CONCLUSION

The judgment of the Circuit Court of Appeals should be affirmed.

Respectfully submitted,

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APPENDIX

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

Nevada Compiled Laws 1929, Vol. 4, Sec. 9463:

In granting a divorce, the court shall also make such disposition of the property of the parties as shall appear just and equitable, having regard to the respective merits of the parties, and to the condition in which they will be left by such divorce, and to the party through whom the property was acquired, and to the burdens imposed upon it, for the benefit of the children. And all property and pecuniary rights and interests, and all rights touching the children, their custody and guardianship, not otherwise disposed of or regulated by the order of the court, shall by such divorce, be divested out of the guilty party, and vested in the party at whose instance the divorce was granted. And if after the filing of the petition, it shall be made to appear probable to the court or the judge, in vacation, that either party is about to do any act that would

defeat or render less effectual any order which the court might ultimately make concerning property or pecuniary interests, an order shall be made for the prevention thereof, to be enforced as such preliminary orders are enforced respecting children.

SEC. 9465:

When the marriage shall be dissolved by the husband being sentenced to imprisonment, and when a divorce shall be ordered for the cause of adultery committed by the husband, the wife shall be entitled to the same proportion of his lands and property as if he were dead; but in other cases the court may set apart such portion for her support, and the support of their children, as shall be deemed just and equitable. In the event of the remarriage of the wife, and there being issue of the former marriage, the court in which the divorce was granted may, on proper showing for cause, enter an order that the alimony previously awarded, or part thereof, be paid as ordered by the court for the benefit of the minor children.

In any suit for divorce now pending, or which may hereafter be commenced, the court or judge may, in its discretion, upon application, of which due notice shall have been given to the husband or his attorney, at any time after the filing of the complaint, require the husband to pay such sums as may be necessary to enable the wife to carry on or defend such suit, and for her support and for the support of the children of the parties during the pendency of such suit; and the court or judge may direct the application of specific property of the husband to such object, and may also direct the payment to the wife for such purpose of any sum or sums that may be due and owing the husband from any quarter, and may enforce all orders made in this behalf, as provided in section 24 of this act.

SEC. 9466:

Whenever an order of divorce from the bonds of matrimony is granted in this territory by the court of competent authority, such order shall fully and completely dissolve the marriage contract as to both parties; and in all suits for divorce brought by a female, if a divorce be granted, the court may, for just and reasonable cause, change the name of such female, and shall in its order decree and appoint.

Connecticut General Statutes, Revision of 1930:

SEC. 5182. *Alimony and change of name.* The superior court may assign to any woman divorced by such court a part of the estate of her husband and, in addition thereto or in lieu thereof, may order alimony to be paid from the husband's income, may change her name and may order alimony pendente lite to be paid to the wife in any complaint or cross-bill for divorce pending in said court. In fixing the amount which shall be allowed, the court shall take into consideration the amount of the husband's income, whether the same is derived from property already acquired or from his personal daily exertions or from both and, whenever an order shall be made for the payment, at stated periods, of alimony from the income of the husband, the court may, at the time of issuing such order, fix a definite amount which may, at any time, be paid by the husband in lieu of all periodical payments which would otherwise accrue after the payment of such amount. Any order for the payment of alimony from income may, at any time thereafter, be set aside or altered by such court. The costs of commitment of any person imprisoned for contempt of court by reason of failure to comply with an order of the court issued under the provisions of this section shall be paid by the state as in criminal cases.

SEC. 5723. *Income of trust fund, to what extent liable to creditors. Expenses of trustee.* Whenever property shall have been given to trustees to pay over the income to any person, without provision for accumulation or express authorization to the trustees to withhold such income, and the income shall not have been expressly given for the support of the beneficiary or his family, such income shall be liable in equity to the claims of all creditors of such beneficiary. Any creditor of such beneficiary may bring an action against him, and any court having jurisdiction may direct such trustees to pay over the net income derived from such trust estate to such creditor, as the same may accrue, until his debt shall be satisfied. When any such trust shall have been expressly provided to be for the support of the beneficiary or his family, a court of equity having jurisdiction may make such order regarding the surplus, if any, not required for the support of the beneficiary or his family, as justice and equity may require. The defendant trustee in any such action shall be entitled to charge in the administration account of such trust such expenses and disbursements as the court to which such action shall be brought shall determine to be reasonable and proper.

SUPREME COURT OF THE UNITED STATES.

No. 427.—October Term, 1939.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, *vs.* Alfred C. Fuller. } On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[April 22, 1940.]

Mr. Justice Douglas delivered the opinion of the Court.

This case raises the question of the circumstances under which income paid to the taxpayer's divorced wife under a trust, the provisions of which have been approved in the divorce decree, is taxable to him. We granted certiorari because of the asserted misapplication by the Circuit Court of Appeals of the rule of *Douglas v. Willcuts*, 296 U. S. 1, to these facts.

On July 25, 1930, respondent and his wife, residing in Connecticut, entered into an agreement in contemplation of divorce which provided, *inter alia*, for the creation by him of a trust of 60,380 shares of Class A common stock of the Fuller Brush Co. The trust was irrevocable and was to continue for ten years. During that period all trust income was to be used for the maintenance and support of the wife, or in case of her prior decease, then for the children; or in case of their prior decease, then for the heirs of the wife or as she should provide in her will. At the expiration of the ten year period the trust property was to be transferred to her outright. The agreement provided for other property settlements, for control and custody of the children, and for waiver by respondent and his wife of all claims against each other arising out of the marital relation. It also contained an agreement on the part of respondent to pay the wife $40 per week for five years, and, if at the end of that period his annual net income exceeded by the amount of the weekly payments the sum of $60,000, to continue those weekly payments for an additional five years or for such portion thereof as his annual net income exceeded the above sum.

The wife repaired to Reno, Nevada, and obtained a divorce decree on November 12, 1930, which "ordered, adjudged, and decreed that

said agreement entered into between the plaintiff and the defendant on or about the twenty-fifth day of July, 1930, be and the same hereby is approved." On December 22, 1930, respondent created the trust provided for in the agreement.[1] The corporate trustee thereunder received from the Fuller Brush Co. all the dividends and income from the trusteed shares during 1931, 1932 and 1933 and disbursed them all for the benefit of the divorced wife. On the failure of respondent to include those amounts in his tax returns for the years in question, the Commissioner assessed deficiencies. The decisions of the Board of Tax Appeals (37 B. T. A. 1233), sustaining the action of the Commissioner, were reversed by the Circuit Court of Appeals. 105 F. (2d) 903.

I. There can be no doubt but that respondent is taxable on the $40 weekly payment to the wife. That is a continuing personal obligation falling within the rule of *Douglas* v. *Willcuts, supra,* as a result of which those payments are taxable to him, not to the wife. *Gould* v. *Gould,* 245 U. S. 151. But that fact does not make the income from the trust also taxable to him. Although the provisions for the weekly payments and for the trust agreement were embodied in the same separation agreement, they were not so interrelated or interdependent as to make the trust a security for the weekly payments. Functionally they were as independent of each other as were the other property settlements from either of them.

II. Petitioner does not challenge the conclusion of the Circuit Court of Appeals that, so far as the trust agreement is concerned, the Nevada court retained no power to alter or modify the divorce

[1] The trust agreement provided that he was to transfer the 60,380 shares of stock on the books of the company from himself personally to himself as trustee and then to deliver the certificate for such shares to the corporate trustee. This was done. Also in accordance with the provisions of the trust respondent executed a dividend order against the shares directing the Fuller Brush Co. to pay all dividends to the corporate trustee. Respondent was the founder of the company and during the years in question was its president. It had outstanding only one class of voting stock, viz. Class A common. The amount outstanding during these years varied between 172,000 and 186,000 shares. Respondent owned 60,380 shares which together with the 60,380 shares under the trust constituted more than a majority of that class of stock. By terms of the trust respondent retained "exclusive voting power" of the trusteed shares during the term of the trust. If he died before its termination, the voting power would pass to the wife. During that period power to sell the stock was vested jointly in him, the wife, and the corporate trustee and could be exercised only in case all three agreed in writing. In case of such a sale, those three had the power to invest and reinvest the proceeds. They also were given the power to disburse, withhold, and accumulate the principal of the trust at their sole discretion, such power over the income being vested in the wife and the corporate trustee.

decree. It seems to be admitted that under Nevada law the wife's allowance once made is final, *Sweeney* v. *Sweeney*, 42 Nev. 431, unless the decree itself expressly reserves the power to modify it, *Lewis* v. *Lewis*, 53 Nev. 398, or unless the decree approves a settlement which in turn provides for a modification. *Aseltine* v. *Second Judicial District Court*, 57 Nev. 269. Here no such power was reserved in the decree or in the trust agreement approved by the decree. Nor did respondent underwrite the principal or income from the trust or any part thereof or make any commitments, contingent or otherwise, respecting them, beyond his promise to transfer the securities to a trustee. But petitioner argues that the rule of *Douglas* v. *Willcuts*, *supra*, should nonetheless apply since the decree recognized the husband's preexisting duty to support and defined that duty as coextensive with what the parties had themselves arranged, and since the husband simply carved out future income from property which he then owned and devoted it in advance to the discharge of his obligation.

We take a different view. If respondent had not placed the shares of stock in trust but had transferred them outright to his wife as part of the property settlement, there seems to be no doubt that income subsequently accrued and paid thereon would be taxable to the wife, not to him. Under the present statutory scheme that case would be no different from one where any debtor, voluntarily or under the compulsion of a court decree, transfers securities, a farm, an office building, or the like, to his creditor in whole or partial payment of his debt. Certainly it could not be claimed that income thereafter accruing from the transferred property must be included in the debtor's income tax return. If the debtor retained no right or interest in and to the property, he would cease to be the owner for purposes of the federal revenue acts. See *Helvering* v. *Clifford*, 309 U. S. —. To hold that a different result necessarily obtains where the transfer is made or the trust is created as part of a property settlement attendant on a divorce would be to hold that for purposes of the federal income tax the marital obligation of the husband to support his wife cannot be discharged. But whether or not it can be depends on state law. For other purposes, local law determines the status of the parties and their property after a decree dissolving the matrimonial bonds. See *Barrett* v. *Failing*, 111 U. S. 523. And while the federal income tax is to be given a uni-

form construction of national application, Congress frequently has made it dependent on state law. See *Thomas* v. *Perkins*, 301 U. S. 655, 659, and cases cited. In the instant situation, an inquiry into state law seems inescapable. For the provisions in the revenue acts[2] and regulations[3] concerning the non-deductibility of "family expenses" and of "alimony" do not illuminate the problem beyond implying the necessity for an examination of local law to determine the marital status and the obligations which have survived a divorce. The Nevada cases tell us that under such a decree as was entered here the obligation to support was *pro tanto* discharged and ended. And the trust agreement contains no contractual undertaking by respondent, contingent or otherwise, for support of the wife. Hence we can only conclude that respondent's personal obligation is not a continuing one but has been discharged *pro tanto*. To hold that it was not would be to find substantial differences between this irrevocable trust and an outright transfer of the shares to the wife, where in terms of local divorce law we can see only attenuated ones. This is not to imply that Congress lacks authority to design a different statutory scheme applying uniform standards for the taxation of income of the so-called alimony trusts. A somewhat comparable statute taxing to the grantor income from a trust applied to the payment of premiums upon insurance policies on his life was upheld in *Burnet* v. *Wells*, 289 U. S. 670. But the reach of Congressional power is one thing; an interpretation of a federal revenue act based on local divorce law, quite another.

For the reasons we have stated, it seems clear that local law and the trust have given the respondent *pro tanto* a full discharge from his duty to support his divorced wife and leave no continuing obligation, contingent or otherwise. Hence under *Helvering* v. *Fitch*, 309 U. S. —, income to the wife from this trust is to be treated the same as income accruing from property after a debtor has transferred that property to his creditor in full satisfaction of his obligation.[4]

III. One other observation is pertinent. Though the divorce decree extinguishes the husband's preexisting duty to support the

[2] Revenue Act of 1928 (45 Stat. 791) § 24(a)(1). The same provision appears in § 24 of the 1932 Act (47 Stat. 169).

[3] Treasury Reg. 74, Arts. 83, 281, promulgated under the 1928 Act. The same provisions appear in Treasury Reg. 77, Arts. 83, 281, promulgated under the 1932 Act.

[4] See Paul, Five Years with Douglas v. Willcuts, 53 Harv. L. Rev. 1.

wife, and though no provision of the trust agreement places such obligation on him, that agreement may nevertheless leave him with sufficient interest in or control over the trust as to make him the owner of the corpus for purposes of the federal income tax. *Helvering* v. *Clifford, supra.*

As we have seen, respondent did retain considerable control over the trusteed shares. But that was not the basis for the assessment of the deficiency by the Commissioner. It was not passed upon by the Board of Tax Appeals or the Circuit Court of Appeals. It was not included in the petition for certiorari among the errors to be urged or the reasons for granting the writ. Nor did petitioner brief or argue the point here. Hence we do not pass on the applicability of the rule of *Helvering* v. *Clifford, supra,* to these facts. Cf. *Helvering* v. *Wood,* 309 U. S. —.

Affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.

SUPREME COURT OF THE UNITED STATES.

No. 427.—October Term, 1939.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, vs. Alfred C. Fuller. | On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[April 22, 1940.]

Mr. Justice Reed, dissenting.

The opinion of the Court in this case is made to turn upon the question whether the law of the taxpayer's residence withdraws divorce settlements from the continuing supervision and subsequent modification of the courts. Two trusts, both irrevocable, in words precisely the same, drawn for the purpose of providing maintenance for former wife, recognized or approved by divorce decrees identical in form, are to have different tax results upon the settlor. If income taxes are predominantly important, prospective divorcés must locate in the states where the finality of the settlement is clearly established. Compare *Douglas* v. *Willcuts*,[1] *Helvering* v. *Fitch*[2] and *Helvering* v. *Leonard*[3] with this case. The reason given to support such a conclusion is that the liability of the settlor for taxes on trust income is based on the possibility that the settlor may be called upon for additional sums in the future. If the obligation continues, the tax liability continues. If the obligation is ended, the tax liability is ended. In *Douglas* v. *Willcuts* continued liability existed. It does not seem to me, however, that this continuing liability was the real basis for the *Douglas* decision. The basis for that decision was the prior appropriation, by the creation of the trust, of future income to meet an obligation of the taxpayer. The following excerpts from pages eight and nine show the foundation for the conclusion:

"Within the limits prescribed by the statute (and there is no suggestion that the provision here went beyond those limits) the court

1 296 U. S. 1.
2 309 U. S. —.
3 No. 426 this Term, decided today.

had full authority to make an allowance to the wife out of her husband's property and to set up a trust to give effect to that allowance."

"Upon the preexisting duty of the husband the decree placed a particular and adequate sanction, and imposed upon petitioner the obligation to devote the income in question, through the medium of the trust, to the use of his divorced wife."

"The creation of a trust by the taxpayer as the channel for the application of the income to the discharge of his obligation leaves the nature of the transaction unaltered. . . . In the present case, the net income of the trust fund, which was paid to the wife under the decree, stands substantially on the same footing as though he had received the income personally and had been required by the decree to make the payment directly."

The *Fitch* case was the first to rely explicitly upon the finality of the settlement. It pushed the idea to the point that the burden was upon the settlor to demonstrate the clear finality of the local settlement. This Court there refused to draw its own conclusion as to what the local law was even though numerous state cases touched upon the subject. In *Helvering* v. *Leonard*, this Court continues to apply the finality rule. It interprets the local law and finds that while "mere property settlements . . . may not be modified" the state judicial reserve power may be exercised where "the provision in the separate agreement, approved by the decree" is for support and maintenance. We are now at the point where the taxability of the settlor depends not only on the "clear and convincing proof" of the finality of the decree but the ability to produce that proof depends upon the skill of the draftsman of the settlement. Fine distinctions are necessary in reasoning but most undesirable in a national tax system.

It is no answer to the problem to say that if the stock had been transferred outright to the wife the husband would not be liable for the tax. If the stock had been kept by the husband and dividends paid as alimony, he would have been liable.[4] Either analogy might be logically followed in the trust situation but the choice of taxability of trust income was made in *Douglas* v. *Willcuts*. That case determines the "general rule."[5]

[4] Gould v. Gould, 245 U. S. 151.

[5] Helvering v. Fitch, p. 6 of slip opinion, decided January 29, 1940.

It may be assumed that the original obligation of the husband to support a divorced wife depends upon state law and to that extent that the state law is applicable to the determination of liability under the federal income tax act. But that necessary reliance upon local law need be carried no farther than the determination of obligation to support. Once that is determined the applicability of the theory of constructive receipt of income to discharge the obligation would come into play and would be nationwide in extent.

The obligation to support exists prior to the divorce decree. It is ended in Nevada only upon getting the court's approval to an arrangement which permits the creation of a fund to meet from year to year the obligation from which the Nevada law then and only then releases the settlor husband.[6] It is by the court's approval that the continuing obligation is discharged. Granting that a lump sum payment would terminate both the marital and the tax liability, the creation of a trust, approved by the court, for continuous payments in lieu of alimony seems to bring the trust income much closer to alimony than to the situation of a final settlement by lump sum payment.

This is particularly true in this present case where the settlement agreement shows that the husband retained voting power over the stock placed in trust. 60,380 shares of Class A Common Stock of the Fuller Brush Company, the only class of voting stock, was placed in the trust. An equal amount was retained by the taxpayer. The aggregate was a majority of the total of voting stock outstanding. This power, retained to the settlor, is of weight in determining that the present trust is more nearly akin to an agreement to pay alimony than it is to a satisfaction of an obligation by an unrestricted transfer.

The judgment should be reversed.

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[6] Nevada Compiled Laws, 1929, §§ 9463 and 9465.